



Effective Retail Promotions

Presentation to

Quick Chek Food Stores

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R. J. Reynolds Tobacco Company

51847 1218

Designing Effective Retail Promotions

Presentation Outline

- ➔ How important are Convenience/Gas outlets for the Cigarette Industry
 - Current Outlet Importance
 - Sales Trends.
- ➔ How do you structure effective promotion offers
 - A word about promotion objectives.
 - Discount values.
 - Determining pack purchase requirements.
 - SIDE BAR: Everyday Multi-Pack Pricing
 - Considering Promotion Profit Rationality.
- ➔ Getting to “Win-Win” Promotion Outcomes?

Effective Retail Promotions

BUSINESS IMPORTANCE AND TRENDS
BY
OUTLET

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- ◆ Convenience/Gas outlets account for nearly half of all cigarette sales.

Percent of Business

Outlets	Cigarette Category		
	Total	Full-Price	Savings
Convenience/Gas	48%	49%	46%
Supermarkets	18%	19%	17%
Discount Member Whse	5%	5%	4%
Drug	5%	6%	3%
Liquor	4%	4%	3%
Cigarette Outlets	11%	8%	19%
All Other	9%	9%	8%

* Based on Calendar 1996 data.

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- ◆ There appears to be a substantial volume shift to convenience/gas (CG) and cigarette outlets (CO) over the last two years.

Cigarette Volume Trends (1995 - 1996)

Outlet	Industry	Full-Price	Savings
Convenience Gas (CG)	+7.4%	+11.1%	-1.9%
Supermarkets (SM)	-15.4%	-13.3%	-20.7%
Discount (DT or MM)	-3.8%	-0.5%	-12.4%
Drug (DG)	-10.4%	-8.4%	-17.9%
Cigarette Outlets (CO)	+32.6%	+42.7%	+22.9%

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THE ELEMENTS OF EFFECTIVE RETAIL PROMOTIONS

Question #1: What is the Promotion Objective?

Designing the “Perfect Promotion” must take into account the Objectives.

Defensive Promotions

- ➔ Promotions designed to defend/hold volume and market share from competitive activity.
- ➔ Inherently unprofitable in the short-term.
- ➔ Focused on the long-term viability of the business.

Offensive Promotions

- ➔ Promotions designed to build the business.
- ➔ Has both a short- and long-term profitability focus.

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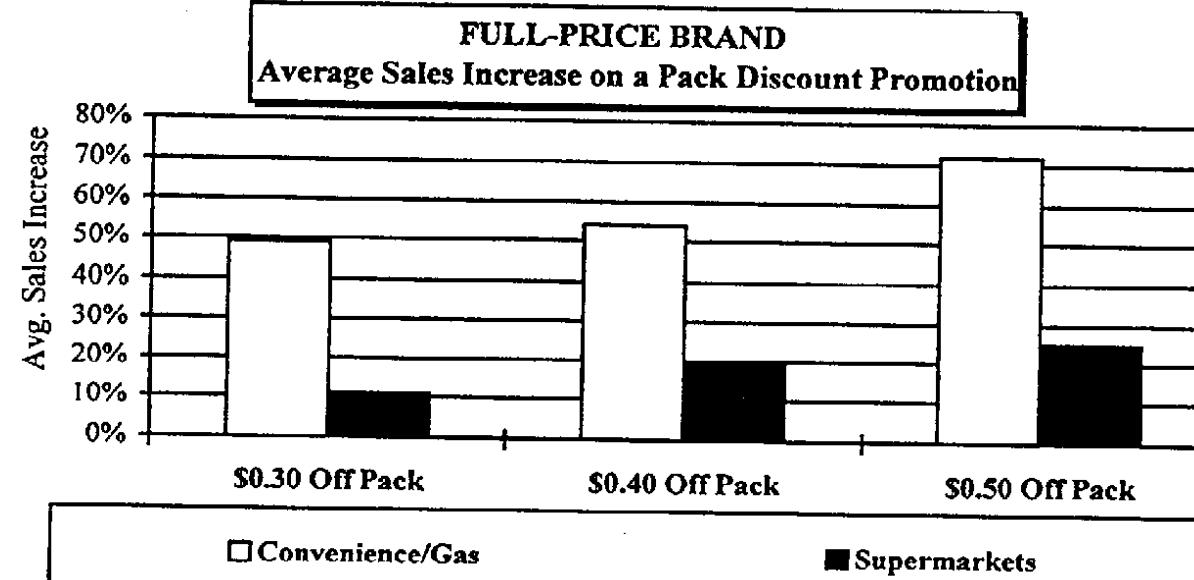
- ◆ Convenience/Gas (CG) outlets are consistently more responsive to retail promotions compared to Supermarkets (SM).

Average Percent Sales Increase on a Retail Promotion

Promotions	Entertainment Brand		Savings Brand	
	SM	CG	SM	CG
Avg. Promotion	46%	56%	44%	71%
Discounts	47%	57%	45%	73%
Premiums	48%	60%	35%	58%

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- ◆ Even on equivalent promotions, response in C/G outlets is substantially greater.



Factors That Drive Promoted Sales Increases

► Increases are driven by a multitude of factors:

- Discount Values or specific program being implemented.
- Specific pack or carton purchase requirements.
- The in-store conditions where the promotion occurs.
- Outdoor communication and advertising.
- Clerk and store manager support.
- Program tie-ins (e.g. sports or local events, co-promotions, etc.).
- The market/geography where the promotion is executed.
- The brand(s) being promoted.
- Promotion clutter in the store.
- Geo-demographics relative to the store location.

Sales Response is Determined by a Multitude of Factors

	Lowest Expected Sales Increase	Average Sales Increase	Highest Expected Sales Increase
\$0.20 Off Pack	15%	30%	75%
\$0.30 Off Pack	30%	49%	96%

Conditions That Create This

Low Promotion Visibility
Weak Promotion Presence
Poor Price Communication
Concurrent Competitive Promotions
High Promoted Price Point

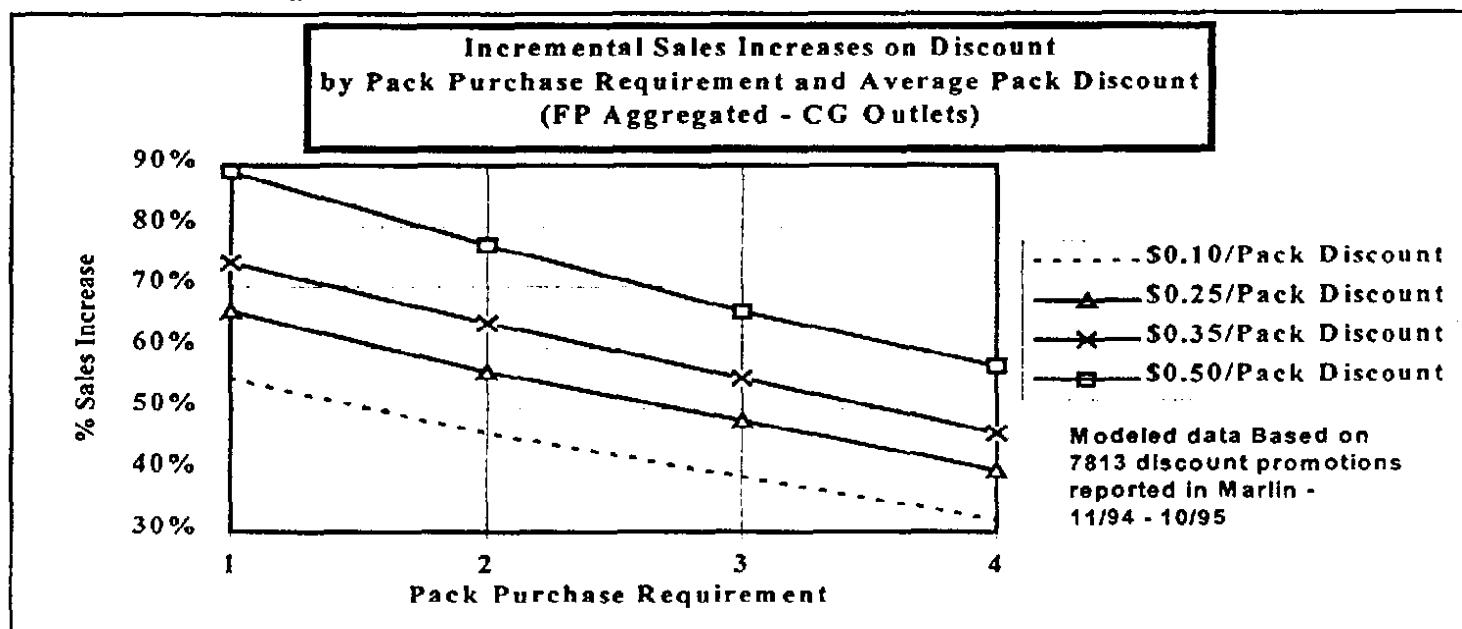
Conditions That Create This

High Promotion Visibility
Strong Promotion Dominance
Clear Price Communication
No Concurrent Competitive Promotions
Low Promoted Price Point

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Discounts & Pack Purchase Requirements

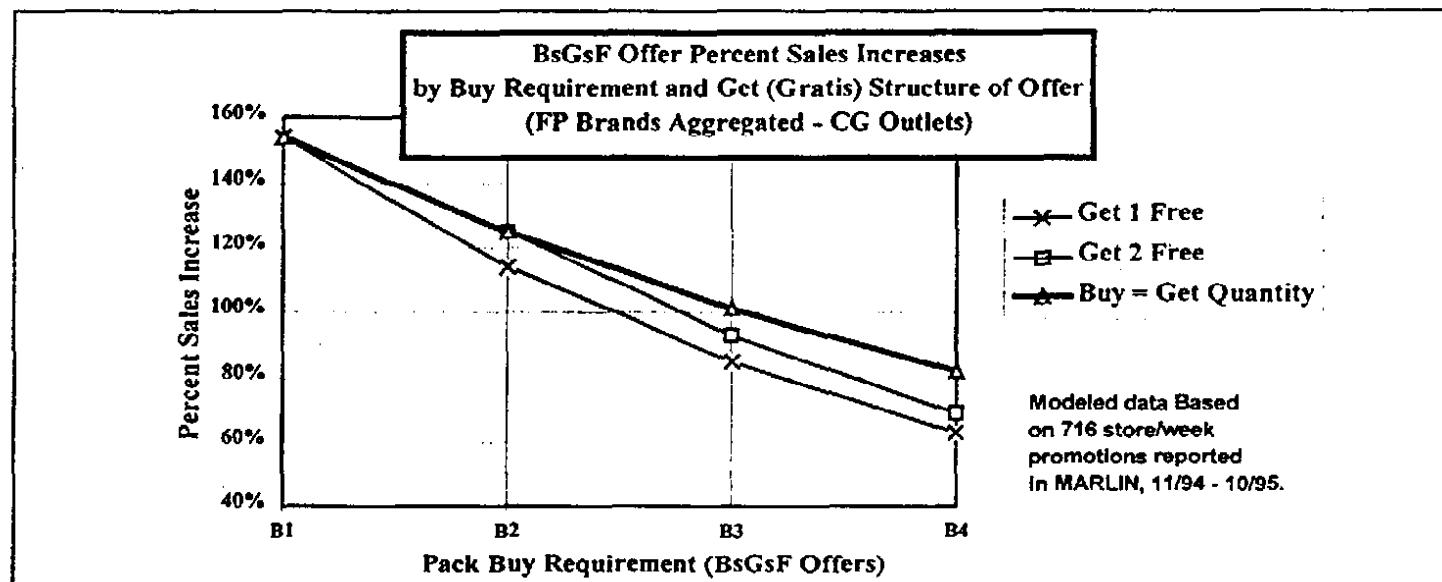
- ◆ Higher discount values lead to greater sales increases.
- ◆ However, even with equivalent per pack discounts, incremental response declines markedly as the purchase requirement increases.



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Pack Purchase Requirements Affect Competitive Participation

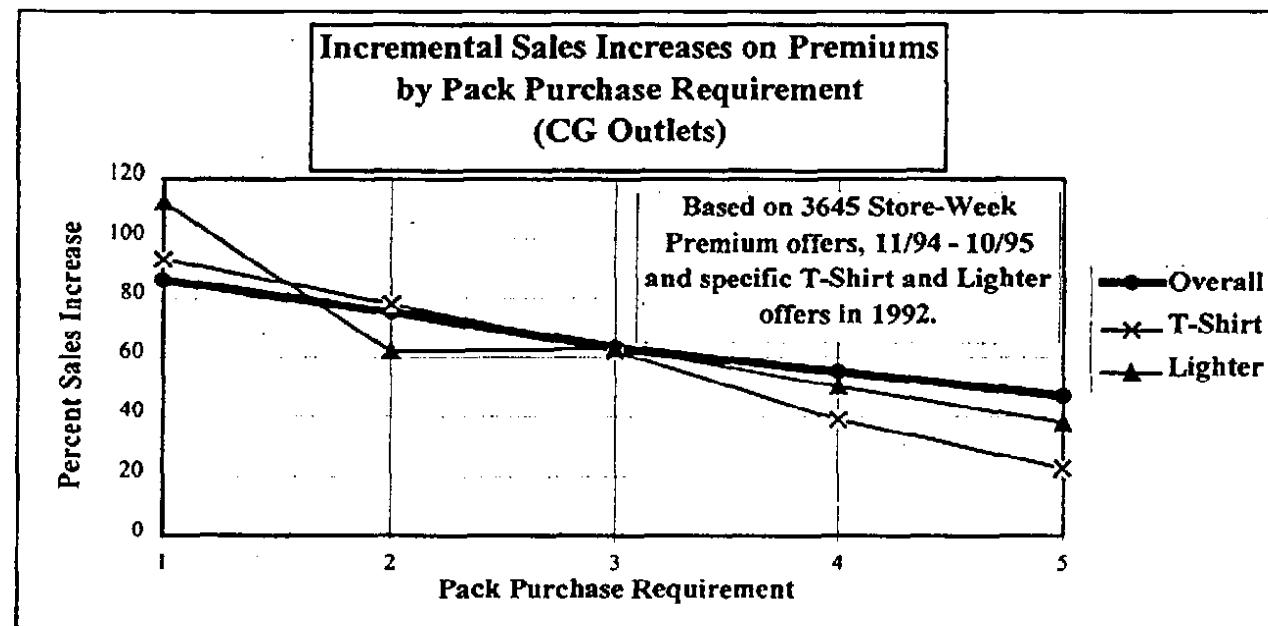
- ◆ The same pattern of promotion response is true of BsGsF offers:
 - Significantly lower response as the buy requirement increases.
 - Greater response to more lucrative promotions.



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Pack Purchase Requirements Affect Competitive Participation

- Similarly, Incremental purchasing on premium offers decline at a rapid rate as the pack purchase requirement increases.



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Cash Outlay Requirements May Affect Promotion Interest

- ◆ The decreased responsiveness related to increased purchase requirements may be the result of a greater than planned cash outlay forced on consumers.
- ◆ We must consider normal purchasing when planning promotions.

Brand	Normal Avg. Pack Purchase	Normal Avg. Cash Outlay per Purchase Occasion	Cost to Consumer: \$0.30/Pk Discount; Pack Purchase Requirement is:		
			1 Pack (\$0.30 TPR)	2 Packs (\$0.60 TPR)	3 Packs (\$0.90 TPR)
Full-Price Brand	1.5 Packs	\$2.93	\$1.65	\$3.30	\$4.95
Branded Savings Brand	1.7 Packs	\$2.47	\$1.15	\$2.30	\$3.45

NOTE: Assumes a Full-Price base price of \$1.95/pack and a \$1.45/pack base price for Branded Savings. TPR = (T)emporary (P)rice (R)eduction.

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SIDE BAR

The Issue of Everyday Multi-Pack Pricing

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Everyday Multi-Pack Pricing

STRATEGY

- Reward consumers with a special price contingent on the purchase of multiple packs of cigarettes.
- Usually requires purchase of 2 - 3 packs on an occasion.
- May be on selected brands or a category wide offer.

Everyday Multi-Pack Pricing

STRATEGIC IMPACT

- ➔ Our experience at Reynolds is that 2 and 3-Pack pricing can be effective if it is well advertised throughout the marketplace
- ➔ This tactic tends to:
 - Pantry load or reward normal purchases of loyal customers.
 - Substantial increment in store traffic if price is lucrative and competitive.
 - Can facilitate shopper loyalty if not matched by competing stores.
- ➔ Since the average CG purchase is 1 - 2 packs, a 3-pack deal may function more as a reward to current buyers.

* 2-packs pricing is better to draw store traffic if the economics allow.

Everyday Multi-Pack Pricing

STRATEGIC RISK

- However, multi-pack pricing is not without competitive risk.
- Strategy can degenerate into a higher cost of business without significant gains if:
 - The value is nominal to consumers - not great enough to induce a store switch.
 - You are matched by competitors, then:
 - * Nominal sales benefits.
 - * Substantial negative profit implications.

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Promotion Profitability

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- ◆ Profitability is a key promotion concern.
- ◆ While discount promotions can lead to substantial sales gains, the margin impact can be negative.
- ◆ The critical question is what sales increase needs to be obtained to breakeven.

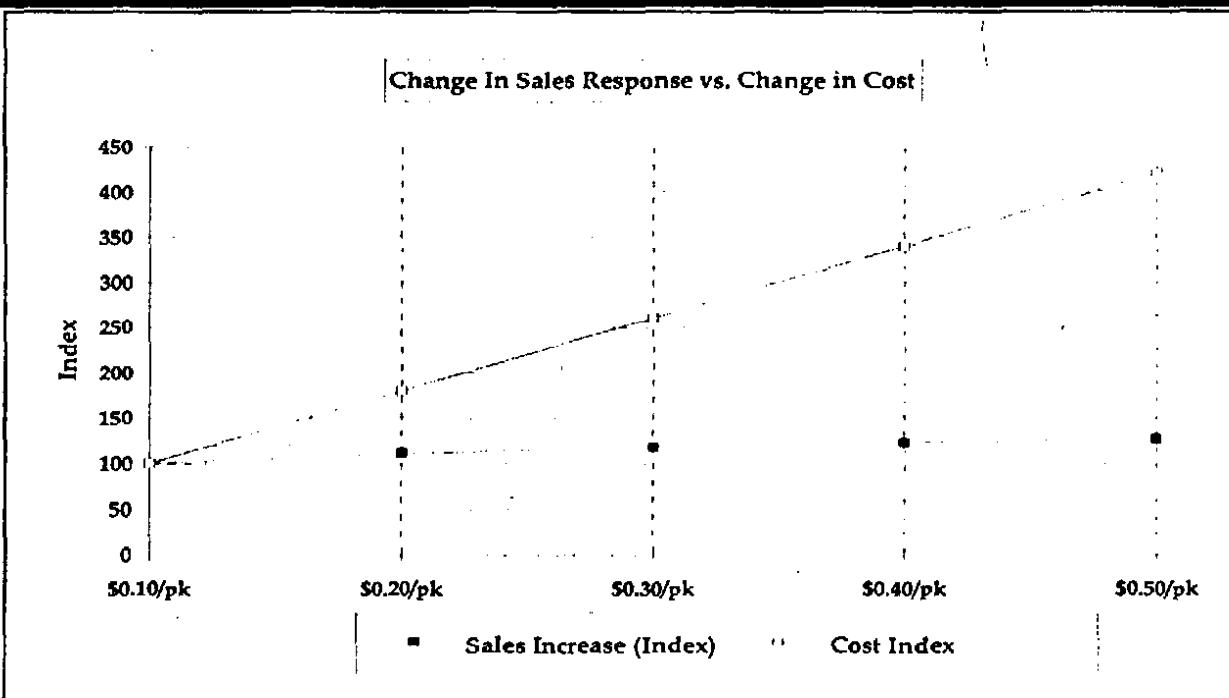
REQUIRED SALES INCREASE TO BREAKEVEN

Discount Offer	Necessary Sales Increase
\$0.20 Off 1 Pack	67%
\$0.30 Off 1 Pack	150%
\$0.40 Off 1 Pack	400%
\$0.50 Off 2 Packs	100%
\$1.00 Off 3 Packs	200%

* Assumes gross margin of \$0.50 per pack.

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- Sales increases spawned by greater discount values generally do not offset the escalated cost.
- We must determine whether a greater strategic or tactical purpose can justify '*below the line*' spending.



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**Getting to Win-Win
Promotion Outcomes**

Getting to Win-Win Promotion Outcomes

- ➔ Mutually beneficial results often require tradeoffs
- ➔ Balancing individual Manufacturer and Retailer perspectives for Win-Win is the key.

Getting to "Win-Win" Promotion Outcomes

Cannibalization Means Different Things to Manufacturers & Retailers

SOURCE OF BUSINESS	True Incremental Sales for the Mfr.	True Incremental Sales for the Retailer
<i>Buyers Who Normally Purchase Cigarettes in the Store Running the Promotion</i>		
Buy their usual brand on deal	NO	NO
Switch from another of the Mfr's brands to the one on deal	NO	NO
Switch to a competitive brand on deal	YES	NO
<i>New Cigarette Buyers for the Store Running the Promotion</i>		
Buy their usual brand on deal	NO	YES
Switch from another of the Mfr's brands to the one on deal	NO	YES
Switch to a competitive brand on deal	YES	YES

Getting to Win-Win Promotion Outcomes

- ◆ As an example, promotion signage may have both upside and downside consequences:
- ◆ Indoor POS signage may:
 - Increase sales on the promoted brand by inducing temporary brand switching (a benefit to the Mfr.).
 - Induce consumers who don't normally buy cigarettes in the store to do so (a benefit to the retailer).
- ◆ Prominent outdoor signage may:
 - Draw consumers into the store who might not normally stop - increasing both cigarette sales and overall ACV (a benefit to the retailer).
 - But, consumers may simply switch outlets with little real gain for the Mfr.
- ◆ The implications are that Win-Win outcomes require tradeoffs, some of which benefit the retailer only and some of which benefit the manufacturer only.

Getting to Win-Win Promotion Outcomes

Cost-sharing programs may help make effective promotions possible

Retailer Benefits

- ➔ More lucrative promotions draw increased store traffic.
- ➔ Goal is to increase total store ACV and profits.

Mfr. Benefits

- ➔ Subsidize unprofitable promotions.
- ➔ More lucrative promotions attract competitive buyers.

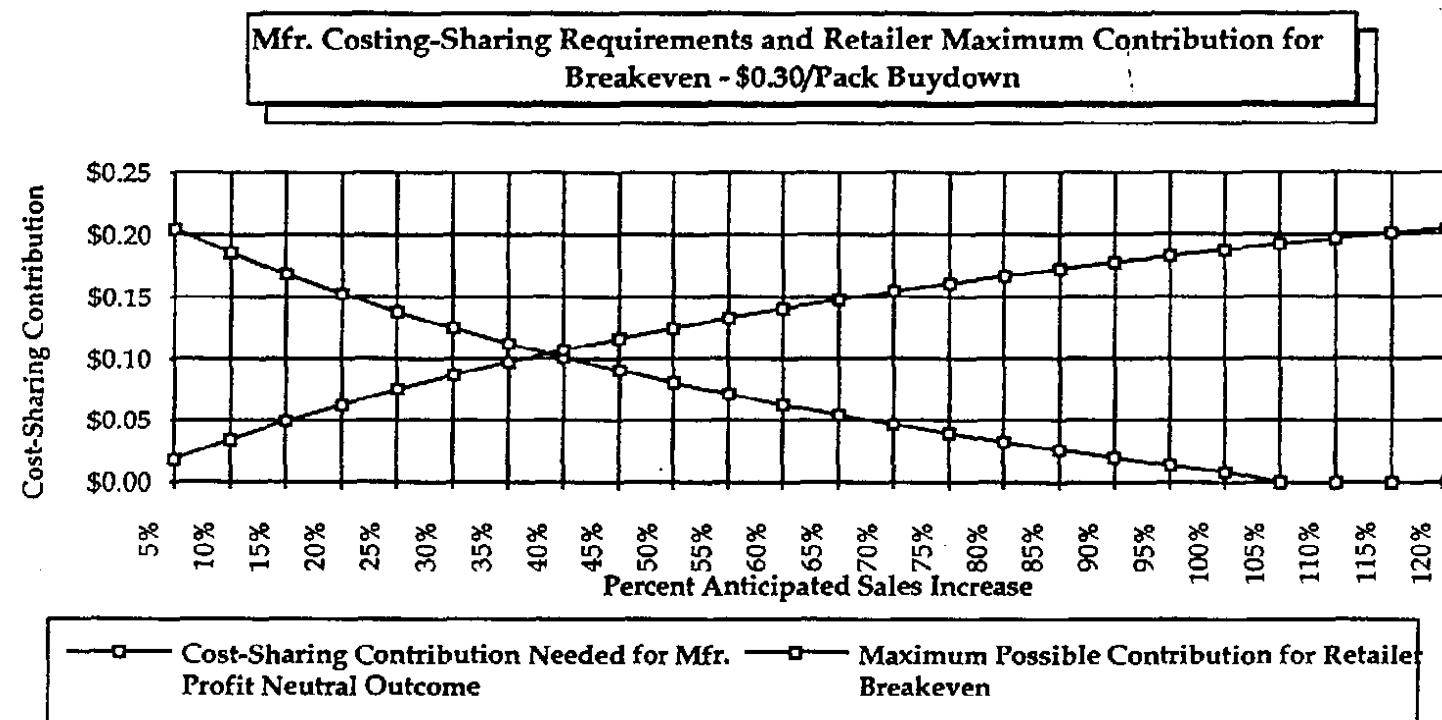
Getting to Win-Win Promotion Outcomes

Effective Cost-Sharing Programs must take into account three factors:

- 1) Promoted sales increases based on the offer value and anticipated factors that affect the incremental gain.
- 2) Mfr. and Retailer Cannibalization/True Incremental Gains:
 - **Mfr.:** True Incremental to the Brand.
 - **Retailer:** True Incremental to the Category & Increased overall ACV.
- 3) Promotion Costs and Cost-Sharing Ratios.

Cost-Sharing Programs Can Be Win-Win Propositions

- The key is to structure a promotion where the minimum contribution the Mfr. needs is compatible with what the retailer can provide.
- The three factors are crucial for this determination



NOTE: Assumes specific Mfr. and Retailer Cannibalization estimates based on the offer and promotion conditions.

Summary Effective Retail Promotions

PROMOTION EFFECTIVENESS REQUIRES

- ◆ Clear objectives be specified and used to plan promotions.
- ◆ Offer values and pack purchase requirements reflect the normal purchasing patterns of consumers.
- ◆ Offer costs are compared to reasonable expectations about potential sales gains or the likelihood of attaining specific strategic goals to determine if the promotion is profit rational.
- ◆ The requirements for Win-Win outcomes are clearly understood and considered when planning promotions.